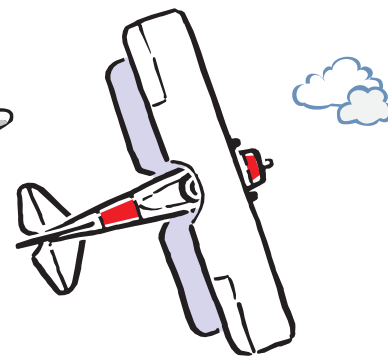


SCHOOL DISTRICT FLYER



Issue 32

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December 2004

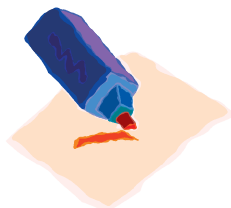
PREVENTING AND DETECTING FRAUD

School district financial statement audits must be performed in accordance with generally accepted auditing standards (GAAS). GAAS now includes Statement on Auditing Standards (SAS) No. 99, *Consideration of Fraud in a Financial Statement Audit*, which is effective for fiscal year 2004 audits. SAS No. 99 establishes standards and provides guidance to audit firms in fulfilling their responsibility, as it relates to fraud, when conducting financial statement audits. As a result, the district's audit firm may be performing additional work to comply with these new standards and guidelines. Most apparent to the districts may be more inquiries of management and staff about the risk of fraud and new or different test work as a result of identified fraud risks. However, SAS No. 99 does not change the audit firm's responsibility in regard to fraud.



GAAS requires that the audit firm obtain reasonable rather than absolute assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud. Accordingly, a material misstatement may remain undetected. Also, an audit is not designed to detect error or fraud that is immaterial to the financial statements.

The responsibility of preventing and detecting fraud still rests with the district. The district must design and implement internal controls to prevent and detect fraud. The policies and procedures provided in the *Uniform System of Financial Records (USFR)* can assist the district in fulfilling this responsibility. However, because of the characteristics of fraud, it may occur even though the controls described in the USFR are in place. Therefore, the district's governing board and management must also create a culture and environment at the district that promotes honesty and ethical behavior.



Finally, when district management becomes aware of weaknesses in the district's internal controls, either through management's own evaluation or deficiencies communicated by the audit firm, management should take steps immediately to correct the deficiencies and strengthen internal controls. Districts may discuss appropriate corrective action with their audit firms or contact our Office for more information.

SCHOOL DISTRICT REPORTING GUIDELINES

We have revised the reporting guidelines for the school district financial statements and related notes for the year ended June 30, 2004. They are available on our Web site. School districts may produce financial statements that vary from these; however, they should be presented in accordance with generally accepted accounting principles.



JTED REPORT RELEASED



The Division of School Audits recently released a special study of the Joint Technological Educational Districts (JTEDs) in Arizona. The report was requested by the Joint Legislative Audit Committee and is now available on our Web site.

QUESTIONS & ANSWERS



Question: May extracurricular activities fees tax credit monies be used for senior trips?

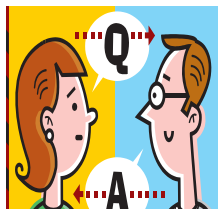
Answer: No. Arizona Revised Statutes (A.R.S.) §43-1089.01(F)(2)(d) specifically excludes senior trips or events that are recreational, amusement, or tourist activities from the definition of extracurricular activities for tax credit purposes.

Question: Does our Office have an approved list of audit firms?

Answer: No. Our Office does not have an approved list of audit firms. However, to assist districts in finding an audit firm, our Office will provide, upon request, a list of audit firms who currently have approved audit contracts with school districts and/or school district-sponsored charter schools and firms interested in contracting for such audit services. Our Office does not recommend, endorse, or vouch for any audit firms on the list. Also, the list is not a prospective bidders' list in accordance with School District Procurement Rules. School districts should refer to *Arizona Administrative Code* R7-2-1023 and R7-2-1062 for more information on compiling and maintaining prospective bidders' lists.

REVISED QUESTION AND ANSWER

The following question originally appeared in our January 2004 issue of the School District Flyer. On August 10, 2004, the Arizona Attorney General's Office issued an opinion on this topic, which supersedes our previous guidance. Therefore, our answer is revised, as follows, to correspond with the Arizona Attorney General's Opinion.



Question: Can an hourly employee's pay be prorated so that equal payments are made each pay period over the school year?

Answer: Yes. Pursuant to Arizona Attorney General Opinion I04-007, all school district employees may request that their compensation be paid over the actual months worked or be prorated in any number of payments as set forth in A.R.S. §23-351(C)(2).

If pay is prorated for hourly employees, districts must have internal controls in place to ensure that hourly employees are paid only for the hours actually worked during the year. Attendance records such as individual time sheets or clock cards should be

prepared for each hourly employee for each pay period, signed by the employee, and approved by the employee's supervisor. The payroll department should review attendance records for any differences between the hours actually worked and the employee's expected hours

(i.e., the number of hours that was used to calculate the employee's annual compensation amount that is being prorated). If an hourly employee has worked fewer hours than expected, the payroll department

should adjust the employee's leave balances. If sufficient leave time is not available, the payroll department should reduce the employee's annual compensation for the hours not worked. If an hourly employee has worked more hours than expected, the payroll department should increase the employee's annual compensation for the additional hours.

The district should base adjustments to an employee's annual compensation on the employee's official hourly rate of pay used to calculate the original annual compensation amount. The district's policies and procedures should specify how it will apply adjustments (i.e., next regular payment of wages, at year-end, etc.) to an employee's compensation. These policies and procedures for applying adjustments should address both continuing employees and employees that terminate during the year to ensure that hourly employees are not over-paid. (Note: If additional hours worked entitles an employee to overtime compensation under the federal Fair Labor Standards Act, the amount of the adjustment must be calculated so as to comply with the Act's overtime requirements.) Employees entitled to overtime compensation must be paid for overtime hours worked no later than 16 days after the end of the most recent pay period in accordance with A.R.S. §23-351(C)(3).



Finally, individual employee files should contain documentation noting whether the employee is electing to receive compensation over the actual months worked or prorated. If pay is prorated, indicate the number of payments and whether compensation due at the end of the school attendance year is to be paid in a lump sum or paid within 2 months after the fiscal year-end.

For more detailed information on proper payroll policies and procedures, see USFR SVI-H, Payroll.

USFR MEMO UPDATE

Since our last newsletter, we have issued USFR Memorandums No. 207-Annual Revenue Budget, No. 208-Fiscal Year 2003-04 Annual Financial Report and Classroom Site Fund Reporting Forms, and No. 209-Increased Sealed Bidding Threshold.



If you need a copy of these or any current USFR Memorandum, please visit our Web site at www.auditorg.state.az.us/manuals_schooldistrict.htm or call the Office's Accounting Services Division at (602) 553-0333.